



The Chartered Tax Adviser Examination

May 2017

Suggested solutions

Human Capital Taxes

Advisory Paper

1.

To: Bob Travers
From: Joe Green
Date: 4 May 2017
Subject: Re Non-resident director

Dear Bob

Jim's residence position is determined using the statutory residence test.

Jim will not be automatically resident or non-resident under the test so his residence position will be determined under the sufficient ties test. This looks at the number of ties that a person has to the UK and the number of days they spend in the UK. I set out an overview below of Jim's ties to the UK:

Tie	Description	2016/17	2017/18
Accommodation	Does Jim have available UK accommodation?	Y	Y
Family	Are Jim's spouse and minor children resident in the UK?	N	N
Work	Does Jim spend 40 days working in the UK (defined as any day where he spends over 3 hours working)?	N	N
91 day	Has Jim spent 91 days or more in the UK (based on where he is at midnight) in either of the previous two tax years?	N	Y

As Jim has not been UK resident before, he can spend up to 183 days in the UK where he has one tie (2016/17) and up to 120 days in the UK with two ties (2017/18):

- For 2016/17, Jim spent 114 days in the UK and therefore retained his non-resident status.
- For 2017/18, Jim will become resident unless he can restrict the number of his UK days.

Implications of tax residence

If Jim becomes tax resident in 2017/18, he will be liable to tax in the UK on either the:

- Remittance basis (UK income and gains and any non-UK income or gains that are brought into the UK), or
- Arising basis (worldwide income and gains per a UK national)

A taxpayer can choose the method that is most beneficial for them depending on their domicile status. This will need to be ascertained.

Remittance basis:

The remittance basis applies automatically if the individual is non-domiciled and non-UK income and gains are less than £2,000. Where non-UK income exceeds this level (as in Jim's case), a claim needs to be made at which point the personal allowance and annual exemption will be lost.

Once Jim has been resident in the UK for seven out of the previous nine tax years, a remittance basis charge would become payable.

Any non-UK income or gains will only be taxable in the UK when it is brought into the UK. This can be in a later year and Jim would need to ensure he is able to track this.

The remittance basis should be considered as Jim can benefit from overseas workday relief for the first three years of residence. Any remuneration relating to duties performed outside of the UK will not be taxable in the UK provided it is paid offshore and not brought into the UK and the conditions below are met:

- The employee was non-resident for three consecutive tax years out of the previous five tax years
- The employee is not UK domiciled
- The remuneration is paid offshore and the employee is taxed on the remittance basis

If overseas workday relief does apply, I would recommend that the company applies for a direction from HM Revenue & Customs to only operate PAYE on the percentage of the employee's total earnings that relate to UK workdays. This will ensure that Jim does not suffer a cash flow disadvantage from potentially being taxed on the same income in two jurisdictions at the same time (ie via payroll withholding in the UK and in New Zealand).

After the end of the 2017/18 tax year, Jim would need to complete a UK tax return to show the actual number of workdays performed and the correct amount of UK taxable earnings.

Jim has a New Zealand bank account into which all his income is paid. This would be classed as a mixed fund. Any funds brought to the UK from this account would be assessed using a prescriptive set of rules at the point the remittance occurred. These rules are expensive and complicated to apply; however, where overseas workday relief applies, special mixed fund rules can be used if certain conditions apply:

- It is a current or deposit account
- If in joint names, only the employee deposits income into this account
- It is located outside of the UK
- It has a balance of less than £10 when employment income is first paid into it.
- It must not have previously been held for earnings eligible for overseas workday relief
- Only employment income is paid into this account
- It is nominated

Remittances from this account would be established on an annual basis and treated as made at the end of the tax year.

Any non-UK income received prior to Jim becoming resident will not be taxable in the UK. Remittances can include cases where a credit card is used in the UK but the bill is settled by funds retained offshore.

Arising basis:

Under UK domestic legislation, once he becomes resident Jim will be UK taxable on his worldwide income. Therefore ADC Ltd should operate PAYE on the full salary that they pay Jim.

When Jim prepares his UK return, it would be necessary to consider the New Zealand/UK double taxation treaty to establish which country had the primary taxing rights and to apply any relief, as appropriate, to prevent double taxation from occurring.

Under Article 4 (2a) of the treaty, Jim's ties will be closer to New Zealand (family have remained there) and therefore New Zealand would have the primary taxing rights.

Under Article 16(1) of the treaty, each country will have the right to tax any workdays carried out in their country; however, as Jim does perform some workdays in New Zealand on behalf of ADC Ltd, it is possible that New Zealand tax will be due on these days. A credit for foreign taxes paid would be claimed on Jim's UK tax return.

Next Steps:

It will be necessary to have a meeting with Jim to confirm his domicile status, discover what his other sources of income are, what funds he may need in the UK and to advise him regarding structuring his bank accounts. Once this meeting has taken place, I will be able to advise him on what basis of taxation would be beneficial.

Kind regards
Bob

MARKING GUIDE

TOPIC	MARKS
Statutory residence test: concluding automatic parts of test don't apply	1
Statutory residence test: overview of Jim's ties to the UK – 2016/17	1
Statutory residence test: overview of Jim's ties to the UK – 2017/18	1
Statutory residence test: concluding on residence position for both years	1
Statutory residence test: advice re residence position and pointers for Jim to consider in 2017/18	1
Residence: setting out that a non-domiciled resident can be taxed in two ways	1
Residence: concluding remittance basis can apply automatically or be claimed	1
Overseas workday relief	2
Company could apply for s.690 direction	1
Highlighting different types of remittances that can be made	1
Identifying Jim's NZ account may be a mixed fund	1
Tax treatment of income received when non resident	1
Special mixed fund rules – explaining conditions and how analysed	2
Arising basis – PAYE obligations	1
Arising basis – treaty analysis	2
Presentation and Higher skills	2
TOTAL	20

2.

To: Aldo Smith
From: Jeremy Bagg
Date: 16 May 2017
Subject: Re New employee proposal

Dear Aldo

Golden Hello payments

A golden hello payment can be paid for the purpose of attracting and rewarding staff or as an inducement payment. The tax treatment will depend on which category it falls into: if it is a reward for future services then it is subject to Income Tax and National Insurance via the payroll. If it is an inducement payment, it may not be taxable if it meets the conditions below:

- It's paid before the employee starts work
- It's not returnable
- It's paid to compensate the employee for giving up some right or asset to take up the employment.

Julian is not giving up some right or asset; he is simply moving employment and relocating for personal reasons. Therefore any golden hello payment will be taxable in full and subject to National Insurance at the point the payment is made. If this is prior to Julian starting work, you will need to register him as a new starter on your payroll software and report any payment made in line with Real Time Information. If Julian cannot provide you with a P45, a new starter checklist would be required to obtain the following information and tax would be deducted using a basic rate tax code:

- Full name
- Date of birth
- Gender
- Address
- Student loan deduction status
- National insurance number

Once the P45 is received, Julian's details should be updated in your payroll software (including the 'Total pay to date' and 'Total tax to date' fields) to ensure the correct tax is deducted going forwards.

If Julian repays the bonus, it will be classed as negative taxable earnings in the tax year in which the repayment is made. If the negative earnings exceed his positive earnings, Julian can make a claim for employment loss relief against general income.

The amount repaid would be income for the company and subject to corporation tax.

Employment-related loan

As an alternative to making a payment to Julian before he joins, you could make a loan of £10,000 to him which could be written off at the end of the set period if Julian is still with the company. There would be no immediate Income Tax or National Insurance implications at the point the loan. If he fails to join or remain with you, the loan would be repaid. If the loan is written off, an Income Tax and National Insurance charge would arise. This would be reportable on form P11d and class 1 national insurance would be collected via payroll.

As the loan won't exceed £10,000, there will be no benefit in kind while the loan is in place, even if the loan is interest free.

Relocation package

Alternatively, a relocation package could be provided as Julian is relocating in order to start work with your firm and in order to reside within a reasonable daily travelling distance of your office. As long as qualifying costs are paid or reimbursed (see below), the first £8,000 could be paid free of Income Tax and National Insurance.

Qualifying costs include assisting Julian with buying/selling his home, moving to Milton Keynes with his family, transporting his belongings and buying replacement items for his new home (such as carpets and curtains that would not be suitable for use in the new home). Paying for Julian and his family to visit the Milton Keynes area on a house hunting visit would also qualify.

Records should be maintained in order to support any claim for exemption and all qualifying relocation costs should be incurred before the end of the tax year following the tax year of the move.

If possible, it will therefore clearly be better for you and for Julian to try to take advantage of this exemption, even though it would mean that payment to him would be delayed until expenses are incurred. As the exemption only applies for the first £8,000 (or such lesser sum as the expenses may be), you would also need to consider how the balance should be paid. You could consider a cash bonus or beneficial loan (for which the treatment would be as outlined above) or you could pay the additional relocation costs on his behalf but these excess costs would either need to be included on form P11d (where paid directly) or through payroll (if reimbursed) and would be subject to tax and national insurance. Where the company contracts and pays for the qualifying costs (as opposed to either reimbursing Julian or paying for services that he has contracted for) Julian would only be liable to the tax due on these costs as the National Insurance (Class 1a) would be payable by the company only and this is therefore a better option for any such costs.

Kind regards

Jeremy

MARKING GUIDE

TOPIC	MARKS
Tax and NIC treatment of Golden Hello payment	1
Setting out conditions why it may not be taxable	1
Applying this to Julian's situation	1
Setting Julian up on payroll if the payment is made before his start date	2
Tax code to use if P45 not yet issued	1
Tax issue on repayment of golden hello	1
Tax and NIC treatment for providing an employment-related loan	1
Tax and NIC treatment on write off of the loan	1
Identifying qualifying relocation costs and preliminary househunting visit	1
Reporting requirements for relocation costs	1
Tax and NIC treatment of relocation expenses (excess)	1
Maintain records to support claim	1
Time limit for claim	1
Presentation and higher skills	1
TOTAL	15

3.

Memo

To: Tax Partner

From: Tax Manager

Subject: UK income tax issues arising from proposed secondment to Alpha plc

I am setting out below my assessment of the UK income tax issues for Astrid as a result of her proposed secondment to the UK.

Residence

In order to determine the extent to which Astrid is within the territorial scope of UK tax, it is necessary to determine her UK tax residence position under the Statutory Residence Test per Sch 45 FA 2013.

We are told the secondment is due to last for at least three years. It will therefore span at least two full UK tax years. Taking the first full UK tax year of the secondment as an example, the facts suggest that she will only be spending one midnight in the UK and two workdays in the UK per week. Allowing for four weeks' annual leave, this gives 48 midnights and 96 UK workdays p.a. As such, none of the automatic overseas tests are met.

Furthermore, none of the automatic UK tests are met either, on the basis that she does not:

- spend more than 183 days in the UK during the year, or
- have a home in the UK, or
- carry out at least 75% of her duties in the UK.

Her residence status will therefore be determined under the Sufficient Ties Test. With 48 midnights in the UK, she will be allowed up to three ties in the UK and remain non-resident. Given that she does not have UK resident family, she does not have an accommodation tie and the country tie is not applicable as she has not previously been resident in the UK, she will only have a maximum of two ties and therefore she will remain non-resident during the course of the assignment.

It is possible that the first or third automatic overseas test may be met in the first or last UK tax years of the secondment, but in this event the conclusion on her residence position remains the same.

As she will remain non-resident in the UK, she will only be taxable on UK-sourced income (i.e. income relating to UK workdays). Furthermore, owing to her role and seniority, there is unlikely to be any scope to argue that the workdays are merely incidental to her overseas role or eligible for relief under the UK-Sweden Double Tax Treaty.

UK tax relief on expenses

Owing to the fact that Alpha plc will be bearing the costs of Astrid's return flights, accommodation and subsistence while Astrid is in the UK, it is necessary to consider the extent to which UK tax relief is available against these reimbursements, as they are clearly in relation to duties carried out in the UK, so are therefore within territorial scope.

Flights and accommodation

UK tax relief is available for the cost of the flights between the UK and Sweden which are borne by the employer under s373 ITEPA 2003 on the basis that:

- Astrid is non-domiciled in the UK, and

- Astrid has been non-resident in the UK in either of the two years prior to the secondment.

The facts suggest both conditions are met. The relief extends to the accommodation provided in respect of that journey (e.g. if it is provided en-route) but not once Astrid has arrived at her destination

Subsistence costs

Tax relief for subsistence may be available under s338 ITEPA 2003 but this will depend on whether it is possible to argue that her workplace in the UK may be treated as a 'temporary workplace'.

Given that her attendance at the UK workplace will be in the course of a period which exceeds 24 months, it will only be possible to consider that the UK is a temporary workplace if the duties are not carried out in the course of a period of 'continuous work', per s339(5)(a) ITEPA 2003. In turn, HMRC consider this to be the case if an individual's attendance at that workplace comprises more than 40% of the total duties carried out over that period. With two workdays a week, it is not clear whether or not this test is met.

If Astrid's work pattern can be managed so that she spends less than 40% of her working time in the UK, then there would be scope to make a claim under s.338 in respect for her UK subsistence costs, but this is open to challenge by HMRC as the 40% test is non-statutory.

If Astrid carries out more than 40% of her duties in the UK, then the UK workplace will be a permanent one and no deduction will be available for subsistence.

MARKING GUIDE

TOPIC	MARKS
<u>Residence</u>	
Astrid is unlikely to meet any of the automatic overseas or UK tests for a full year on secondment (although likely to be meet 2 nd automatic overseas test for first and last year)	½
Explaining why none of the automatic overseas or UK tests are met	1½
Sufficient ties test (for a full-year on assignment): 90-day – no (assumed) Work – yes Accommodation – no (assuming hotel not block-booked) Family – no Number of midnights – c. 48 (1x(52-4)) p.a. based on facts assuming 4 weeks' annual leave. So non-resident. [Examiner note: if candidate concludes Astrid is resident in the UK on alternative assumptions, they should proceed to consider her treaty residence position and conclude she is treaty non-resident under Article 4. Up to 4 marks should be available for sound logic.]	2
As Astrid is (treaty) non-resident in the UK she will only be taxable on income relating to her UK workdays (which are clearly substantive)	1
<u>Tax relief on expenses</u>	
Expense reimbursements clearly in relation to UK duties, so within territorial scope.	1
Tax relief for costs of flights should be available under s.373 (1) assuming non-domiciled in the UK (1/2) and non-resident in either of 2 years prior to secondment (1/2)	2
Tax relief under s.373 does not extend to accommodation (unless provided en-route) or subsistence.	1
Tax relief under s.338 for subsistence will depend on whether we can treat the UK as a 'temporary workplace'	1
Facts suggest her attendance at the UK workplace will be over a period longer than 24 months, so question is whether duties are in the 'course of a period of continuous work' (s. 339(5)(a)).	1
HMRC considers this test to be met if more than 40% of duties are carried out at that place over the period	1
Facts suggest her attendance is around this level (2 workdays a week), so it is not clear whether this test is met.	½
If Astrid's work pattern can be managed so that she spends less than 40% of her work in the UK, then there would be scope to make a claim under s.338 re. UK subsistence (1), but this is open to challenge by HMRC as the 40% test is non-statutory (1/2).	1½
If Astrid spends more than 40% of her duties in the UK, then the UK workplace will be a permanent one and no deduction will be available for subsistence.	1
TOTAL	15

4.

UK tax advantaged share plans – outbound

Memo

To: Tax partner
Re: PPT Plc share plan participation by outbound assignee “Emily”

Tax residency for Double Tax Agreement purposes

For the period 1 January 2017 through to 5 April 2017 Emily will be considered resident in both the UK and Germany under their respective domestic rules. We must use the Article 4 treaty tie break test to determine in which of the two countries she will be considered resident for the purposes of interpreting the double taxation agreement (AKA Treaty resident).

Using this test, Emily is considered treaty resident in the UK for this period on the basis that she only has a permanent home available to her in the UK.

The OECD definition of “permanent home” refers to a dwelling that is available to the individual at all times continuously, and not only occasionally for the purpose of a stay. The UK leased apartment would qualify but the hotel rooms in which Emily spends two nights a week would not.

For the period 6 April 2017 to 5 April 2018 Emily is only tax resident in Germany so will automatically also be considered resident in Germany for the purpose of interpreting the treaty.

Impact of assignment on CSOP

A CSOP is only tax advantaged for UK purposes. German tax rules will be different. We would strongly recommend taking advice from a German tax professional.

Emily’s eligibility to continue to participate in the CSOP

A non UK resident can participate in a CSOP as long as they are an employee of the company. Emily can continue to participate in the CSOP throughout her assignment.

Options awarded during German assignment

There should never be a charge to UK income tax on the grant of an option under a CSOP as it should not be possible to grant options at undervalue under the plan’s rules.

Income tax treatment of option exercise and share sale during German assignment

Emily will only be eligible to exercise the options granted to her in June 2014 as these are the only options that will have met the three year minimum vesting period imposed under the CSOP rules while she is on assignment to Germany.

Emily does not need to be UK tax resident for the exercise to qualify for UK tax advantaged status. As such there will be no UK income tax on the exercise.

Capital gains tax treatment of share sale during assignment

As Emily is considered non-resident for UK tax purposes in the 17/18 tax year she will not be subject to UK capital gains tax on the sale of the shares.

Additionally this sale will not fall within the temporary non residence rules for CGT even though she will spend fewer than 5 years as a non-resident. This is because she will have both acquired (through the option exercise) and sold the shares in a full tax year of UK non-residence.

Trailing liability to German taxes

It is worth noting that as Emily will have been taxable in Germany on her employment income for part of the vesting period of options granted both before and during her German assignment there may be a trailing liability to German income tax on the exercise of these options even if this is some years after she has returned to the UK. Advice should be sought from a German tax professional.

As Emily is fully tax equalised on her employment income throughout the period of the assignment any German taxes payable at the time of the assignment and relating back to the period of the assignment will be a cost to PPT Plc.

If Emily is UK tax resident at the time German income taxes are paid on her behalf they will be additional taxable UK employment income. The additional UK taxes payable on this should also be considered a cost to PPT Plc.

German income taxes payable on the acquisition of the shares may be taken as a foreign tax credit against the UK capital gains tax charge on their sale. Any reduction in the UK CGT liability as a result of this should be to the benefit of PPT Plc and Emily should make a payment to PPT Plc equal to the reduction in her capital gains tax liability.

MARKING GUIDE

TOPIC	MARKS
<p><u>Tax residency for Double Tax Agreement purposes</u></p> <p>1 January 2017 through to 5 April 2017 Resident in both countries so must use the treaty tie break test. Discussion of permanent home. Conclusion of UK treaty residence.</p> <p>6 April 2017 to 5 April 2018 Only resident in one country so automatically treaty resident in that country Conclusion of German treaty residence.</p>	<p>1 1 ½</p> <p>1 ½</p>
<p><u>Impact of assignment on CSOP</u></p> <p>CSOP is only tax advantaged for UK tax purposes. A non UK resident can participate in a CSOP No UK taxes on grant of option Only eligible to exercise options >3y since grant No UK income tax on the exercise NR at sale therefore no CGT. Discussion of why temporary NR rules do not apply to these shares Discussion of potential trailing liability to German taxes and potential for FTC against UK CGT Discussion of impact of tax equalisation on share based remuneration</p> <p>Presentation & higher skills mark</p>	<p>1 1 1 1 1 1 1 1 2 1</p>
Total	15

5.

Social security – individual leaving the UK

Memo

To: Payroll manager

Re: Social security and payroll issues during Paul Massey's assignment to South Africa

Paul's UK social security position while in South Africa

UK NIC continues to be due for the first 52 weeks that Paul is working abroad.

This is because Paul continues to be employed by an employer with a UK place of business, is resident (for social security purposes) immediately before leaving the UK, and continues to be ordinarily resident in the UK (for social security purposes) throughout the assignment.

During this period, employee and employer Class 1 NIC will be due on all cash payments made to Paul including his Cost of Living Allowance.

It will also be due on any income taxes or employee social security payments which are made by UIH Ltd or the South African company on Paul's behalf. Class 1 employer NIC does not need to be included in Paul's income as this is a liability of the employer rather than the employee.

If Paul is provided with an accommodation allowance by UIH Ltd this will also be subject to Class 1 NIC.

If the apartment is leased directly by the company no Class 1A contributions will be due on this benefit as long as Paul has no taxable duties in the UK during the period he has an ongoing NIC liability. This is because there can be no charge to Class 1A NIC where there is no income tax charge on that benefit.

After the initial 52 weeks, there is no mandatory NIC liability in the UK for Paul. However, voluntary contributions can be made by paying Class 2 NIC.

Paul's personal liability for social security while on assignment

Throughout the three years of the assignment Paul's gross salary will be reduced by "hypothetical NIC" calculated as if he had not left the UK. This hypothetical NIC will be Paul's personal liability.

UIH's liability for social security during Paul's assignment

UIH will be liable for any actual social security payments due throughout the assignment. The cost of this will be offset by the hypothetical social security withheld from Paul as discussed above.

UIH's liability includes the UK Class 1 employee and employer contributions during the first 52 weeks of the assignment, any South African social security payments necessary, and as per their undertaking to do so, the cost of any Class 2 contributions needed to maintain Paul's state pension contribution record.

Payroll obligations for UIH Ltd in respect of Paul while he is in South Africa

The "NT" code is for PAYE income tax purposes, it does not stop NIC withholding. The company must continue to remit Class 1 employer and employee NIC liabilities to HMRC via the UK payroll for the first 52 weeks of the assignment.

It can be complicated to operate UK payroll covering an ongoing UK NIC liability for outbound tax and NIC equalised employees. There is a high chance that mistakes will be made or overseas tax payments will be reported late exposing UIH Ltd to late payment penalties and interest.

UIH Ltd should consider applying to HMRC to operate an Appendix 7b modified payroll agreement. This would allow UIH Ltd to make estimated monthly Class 1 NIC payments to HMRC via the main PAYE scheme for the company. After the year is over they would then complete a final reconciliation based on accurate details of earnings and an EP APP7B NIC Settlement return. The NICs Settlement Return and any balancing payment should be submitted to HMRC by 31 March following the end of the tax year.

In order to qualify to be included on an EP Appendix 7B NICs Settlement Return Paul must meet the following qualifying conditions

- He must be employed by a UK employer and have been assigned to work abroad for a limited duration, but for more than a complete tax year
- He must have an ongoing liability to UK NICs whilst abroad
- He must earn above the upper earnings limit in every earnings period throughout the tax year
- He must be non-resident for tax purposes and not liable to UK tax on his earnings from his employment
- He must receive some earnings and benefits derived from the employment from sources other than the UK employer

Paul would appear likely to be eligible for this scheme.

MARKING GUIDE

TOPIC	MARKS
<u>Paul's UK social security position while in South Africa</u> Identification and explanation of ongoing liability to UK NIC Class 1 NICs due on salary and cash allowances Discussion of payments to be included in Class 1 NIC gross up calculation. Discussion of NIC treatment of accommodation provision Discussion of post 52 weeks and voluntary contributions	2 1 1 2 1
<u>Paul's personal liability for social security while on assignment</u> Discussion of hypothetical NIC.	1
<u>UIH's liability for social security during Paul's assignment</u> Identification and discussion of UIH's responsibility to make all actual social security payments	1
<u>Payroll obligations for UIH Ltd in respect of Paul while he is in South Africa</u> Discussion of "NT" code and ongoing requirement to remit UK NIC in respect of Paul via the UK payroll. Appendix 7b modified payroll agreement recommendation. Appendix 7b explanation – monthly estimates, end of year reconciliation return, payment due date. Appendix 7b explanation - qualifying conditions and assessment of Paul's eligibility Presentation mark	1 1 1 2 1
TOTAL	15

6.

To: Michael Atkinson
From: Anne Adviser
Date: 1 May 2017
Subject: PAYE Review

Dear Michael,

Thank you for your email.

Employed or Self Employed?

I note that Fred has signed a declaration that he is self-employed and will personally report his income and taxes to HMRC via Self Assessment. However, the company cannot rely on this when considering withholding or reporting obligations. The responsibility for determining whether an individual is employed or self-employed rests with 4rail Ltd as the engager.

Legislation does not define whether someone is employed or self-employed. There are however a number of factors derived from cases that have been considered by the courts which provide the starting point for determining status. The following factors need to be considered.

Mutuality of obligations

An employee typically has a contract of employment which dictates the terms under which the engager must provide and pay for work and that the worker is under obligation to accept and perform the work.

Fred has a contractual obligation for minimum hours worked which would indicate employment status.

Right of control

An employee will have very little control over what they do on a day to day basis. Fred can prioritise his work and choose the days he works, which indicates self-employed status.

Provision of own equipment

An employee is rarely responsible for providing tools or equipment, but a self-employed person would customarily do so.

All equipment is provided to Fred, this indicates employment status.

Right of substitution

An employee will not typically have freedom to provide a substitute or engage helpers, but a self-employed person could do so. There is no indication that Fred is able to do this.

Financial risk

The risk of making a loss is a strong indicator of self-employment and can be a decisive factor on its own. Fred does not bear any risk of loss as he has no overheads and 4rail Ltd provide him with everything required to perform tasks. This fact strongly indicates employment status.

Opportunity to profit

A person whose profit depends on the capacity to reduce overheads and organise work effectively is likely to be self-employed. Fred does not appear to have the capacity to increase his profitability which would indicate employment status.

Degree of Integration

An employee will usually be 'part and parcel' of the organisation and integrated into the business. For example, an employee will usually have their own desk or workspace. There is no evidence of this factor here.

Right to terminate contract

A right to terminate an engagement by giving notice of a specified length may be indicative of employment. Fred and the company have a one month notice period which would indicate employment status.

Number of paymasters

An employee typically has one paymaster, but a self-employed person typically provides services to a number of engagers. There is no evidence of this factor here.

Other relevant factors

Fred invoices the company at regular monthly intervals and is paid by the same date each month.

An employee will generally receive payment at regular intervals. This factor indicates employment status.

Conclusion

Fred's only indicators of self-employment status are that he has autonomy over the priority of the tasks he performs and the days he works.

On consideration of all factors, Fred is likely to be considered an employee. As a result, 4rail Ltd should have been;

- deducting Income Tax at source from the payments made,
- deducting Class 1 primary NICs from the payments, and
- paying Class 1 secondary NICs on the payments via PAYE.

Fred's rights should also be protected under employment law for such things as statutory sick pay, statutory paternity pay, holiday pay, the right not to be dismissed unfairly or without notice, the right to join the company pension scheme etc.

Company Van and Fuel

As Fred should be regarded an employee for tax purposes, it is necessary to consider whether the provision of a company van and fuel is a taxable benefit.

There is no taxable benefit where the 'restricted private use' condition is met. The 'restricted private use' condition is met if:

- the terms under which the van is available prohibit private use other than for the purposes of ordinary commuting, or the extent to which not satisfied is insignificant, and
- the primary reason that the employee has the van is because it is required for business travel in the normal course of their duties.

From the information you have provided, this condition is met and so no benefit arises on the van or the provision of fuel.

PAYE and NIC failure

As the employment has taken place in the previous tax year, the company will have a PAYE and NIC failure for 2016/17. I have estimated the PAYE and NIC payments due below.

25 hours x 52 weeks x £25 per hour = £32,500

PAYE = £32,500 - £11,000 = £21,500 x 20% = £4,300

Employee's NIC = £32,500 - £8,060 = £24,440 x 12% = £2,933

Employer's NIC = £32,500 - £8,112 = £24,388 x 13.8% = £3,366

Subject to HMRC's confirmation that Fred is entitled to the full personal allowance, the PAYE and NIC underpayment for 2016/17 is £10,599. Interest will be due from the dates on which the normal PAYE and NIC monthly payments should have been made during the year.

Disclosure and Penalties

You should make a disclosure to HMRC as soon as possible. The timing and quality of a disclosure of a PAYE and NIC failure to HMRC is important to mitigate penalties. Penalties are calculated as a percentage of potential lost revenue (the £10,599 calculated above).

It is likely that in this case, HMRC will argue that the company has been 'Careless'. If the disclosure is 'unprompted', the penalty percentage range is 0 to 30%.

If the penalty is above the 0% minimum, then it can potentially be discounted by up to 100% by:

- 30% voluntary disclosure,
- 40% for helping HMRC resolve, and
- 30% for allowing HMRC access to records.

Finally, the company should seek to recover the PAYE and NIC underpayments from Fred, otherwise the amounts paid to Fred would need to be treated as net payments and tax and NIC would need to be calculated on a grossed up basis.

Kind regards.

Anne Adviser

MARKING GUIDE

TOPIC	MARKS
Identify cannot rely on declaration made by contractor	½
Identify company responsibility for identifying employment status	½
Identify no single test, but decided by case law	½
Identify that status is determined by reviewing all factors and weighting is a factor	½
Mutuality of obligations - identify factor here indicates employment	1
Right of control - identify autonomy over priority and days indicating SE	1
Provision of own equipment - identify factor here indicates employment	1
Right of substitution – identify no factor here	½
Financial risk – identify factor here indicating employment	1
Opportunity to profit – identify factor here indicating employment	1
Degree of integration – identify no factor here	½
Right to terminate contract – identify factor here indicating employment	1
Number of paymasters – identify no factor here	½
Other factors – identify regular payments indicating employment	1
Draw conclusion of Employment status	½
Identify impact of employment status, ½ mark for each of (PAYE for IT – EENIC - ER NIC - Employment rights)	2
Identify company van and fuel considerations, rules and evaluation that based on facts, van and fuel benefits will be £nil	1½
Identify PAYE failure - calculate estimated tax - EE NIC - ER NIC	1½

Voluntary disclosure – interest – likely penalty position – discounts available	2
Identify potential to recover Income Tax and EE NIC from Fred and impact of not	1
Presentation & Higher skills	1
TOTAL	20